

Industry Perspective

Panel: State of B.C.'s Forest Industry
Council of Forest Industries
Annual General Meeting and Conference

April 14, 2005



The B.C. Forest Industry

The B.C. Forest Industry is Focused in Five Primary Commodity Groups:

- Market Pulp
- Newsprint
- Printing Papers
- Paperboard
- Wood Products (lumber and panels)

Normalized Shipments and Value of B.C. P&FP Industry Products

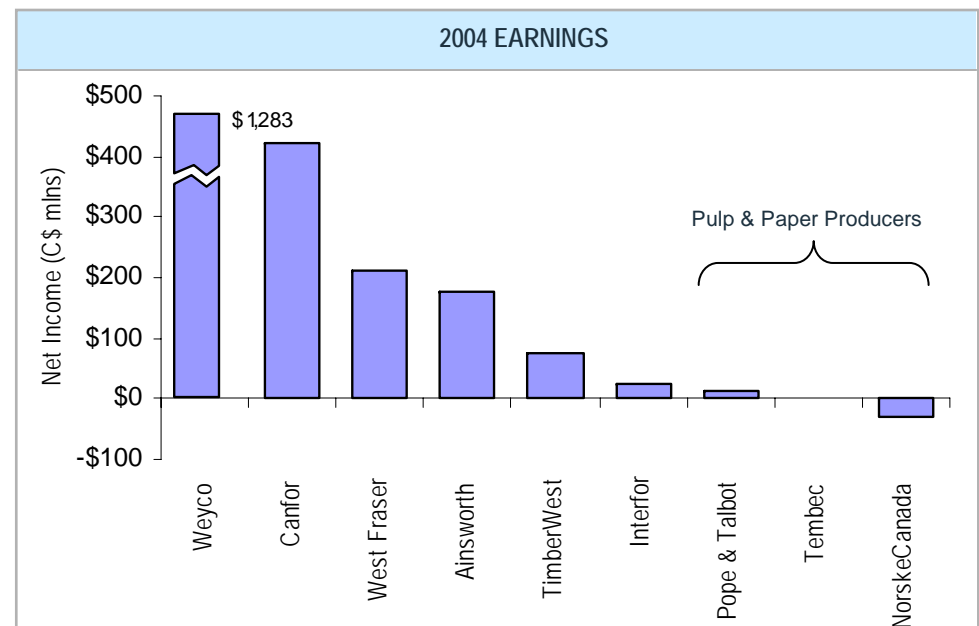
	Pulp	Newsprint	Other Paper & Paperboard	Lumber	Panels	Other Operations	Total
	----- (000 tonnes) -----			(mmfbm)	(mmsf (3/8"))		
Shipments (000s)	4,500	1,200	1,600	13,700	3,000		
Value (mln\$)	\$3,000	\$1,400	\$1,250	\$8,500	\$1,000	\$4,500	\$19,650
% Total Value	15%	7%	6%	43%	5%	23%	100%

Things are Good... Aren't They???

The fact is, things have been VERY good (if you are a wood products producer)!!!

- Wood Products demand has been very strong with pricing at cyclical highs
- Wood products producers have experienced near-peak earnings
- Pulp and paper producers have badly under-performed

B.C. PUBLICALLY TRADED P&FP COMPANIES – EARNINGS			
	2004	2003	2002
Ainsworth	\$175.1	\$123.7	(\$17.9)
Canfor	\$421.0	\$153.0	\$12.0
Interfor	\$25.0	(\$23.0)	\$40.0
TimberWest	\$76.9	\$24.8	\$39.3
Tembec	\$1.0	\$11.0	(\$116.0)
West Fraser	\$212.0	\$33.0	\$138.0
Weyerhaeuser	\$1,283.0	\$277.0	\$241.0
Pope & Talbot	\$14.0	(\$35.0)	(\$33.0)
NorskeCanada	(\$29.0)	(\$85.0)	(\$123.0)



Good Times in Wood Products Have Mostly Been Well Spent...

- Smart wood products producers now have relatively healthy balance sheets (ready to weather a storm)
- Some appear to have “bet the farm”
- “Pulp and Paper” producers generally have weak balance sheets and even worse trajectories
- History suggests this is not an industry to run with an exposed balance sheet!

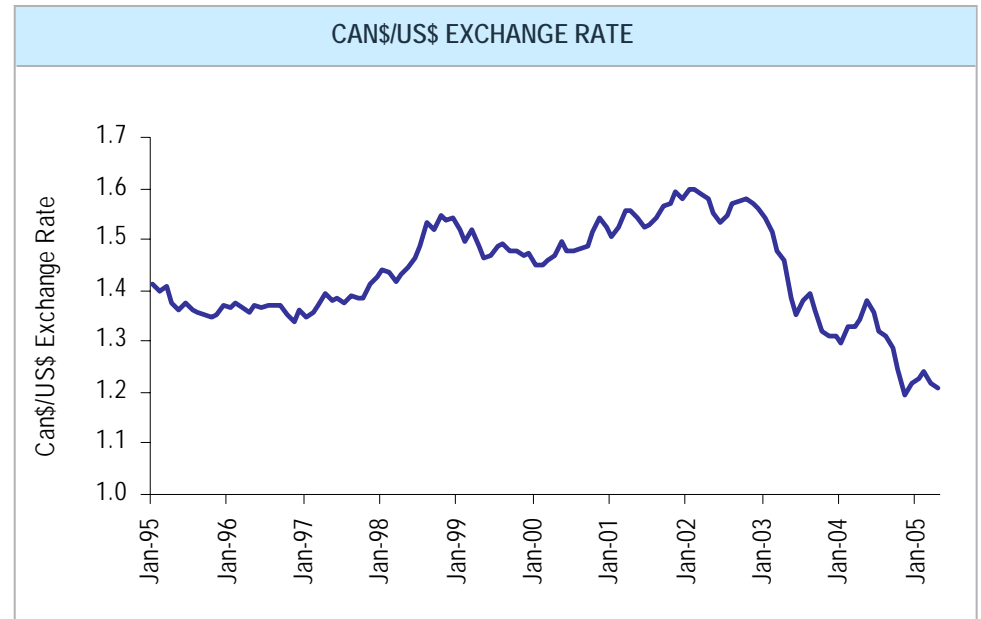
B.C. PUBLICALLY TRADED P&FP COMPANIES - BALANCE SHEET

	D/D+E (Dec 2004)	EBITDA/Interest (2004)
Canfor	19%	13.4
TimberWest	19%	6.5
Interfor	20% ¹	34.2
West Fraser	23%	27.6
NorskeCanada	43.3%	2.0
Weyerhaeuser (US\$)	54%	5.0
Tembec	57%	1.2
Pope & Talbot	58%	3.6
Ainsworth	75%	9.3

¹Interfor is estimated post Floragon acquisition

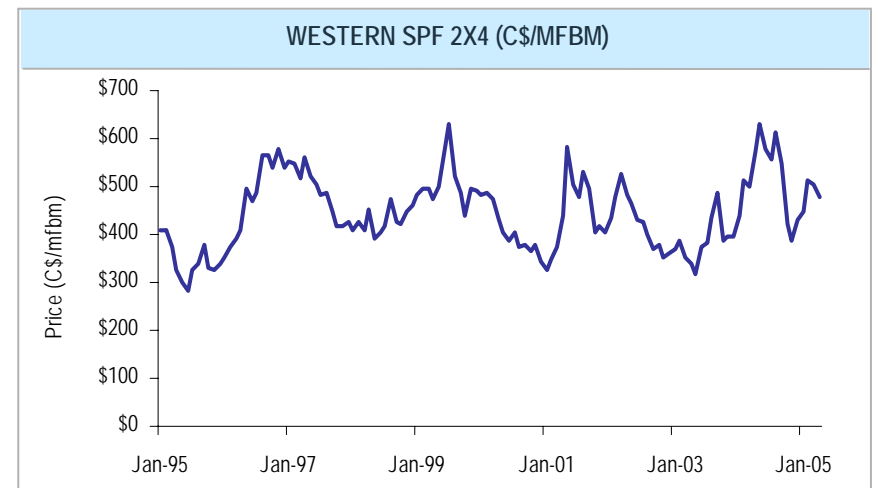
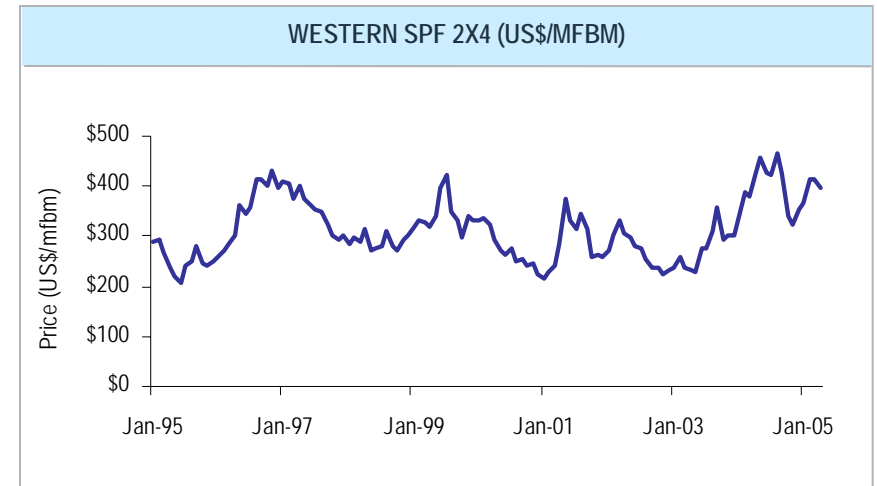
Strong Commodity Prices have Offset the Weak US\$

- The combination of significant Can\$ appreciation and onerous countervailing and anti-dumping duties might have been expected to deliver a knock-out punch to the Canadian P&FP's industry
- An increasingly strong global economy and increases in US\$ based prices for most commodities have meaningfully offset these challenges
- Such good fortune should not be taken for granted!



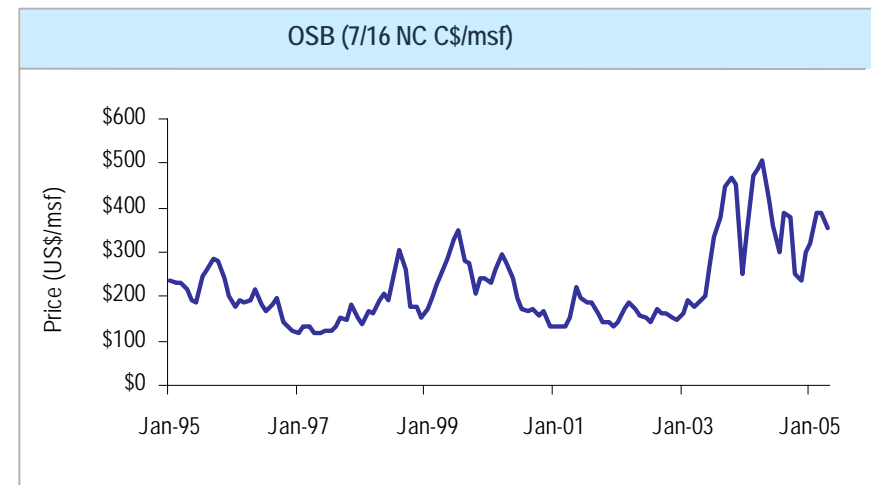
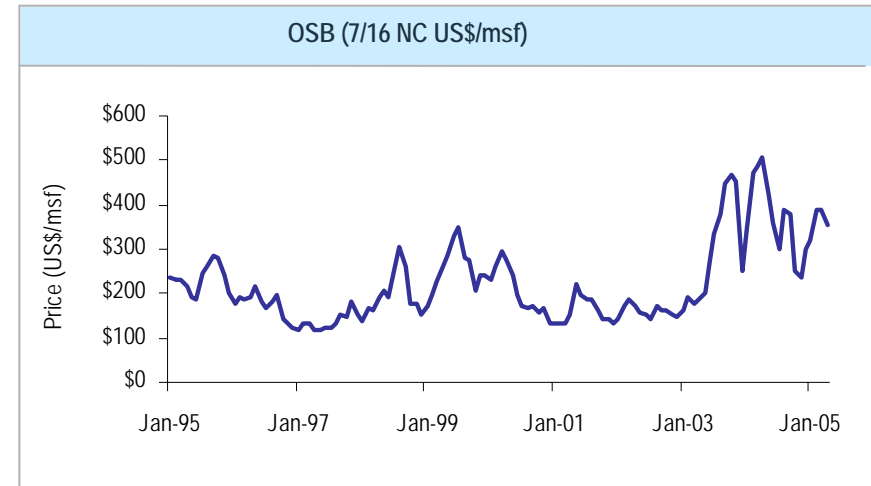
Lumber Prices have Been Above Trend in Canadian Dollars

- Lumber Producers have benefited not only from pricing at, or above 10-years highs, but also from very strong demand, allowing
 - Interior producer to sell increased production, largely passing on costs of duties; and
 - Producers to benefit from improved capital utilization
- Canadian dollar prices have averaged C\$69 (16%) above the 10-year average over the past 15 months
- Credit for much of the industry's strong performance must go to the efficiencies of the BC Interior industry



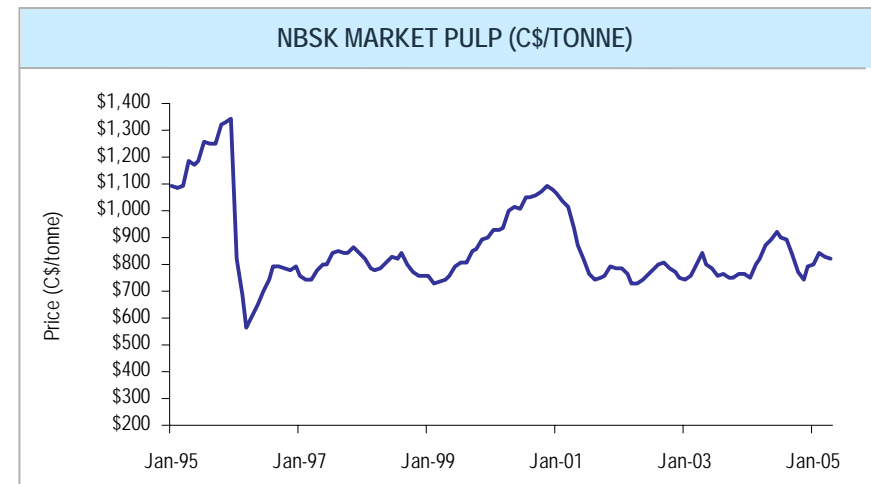
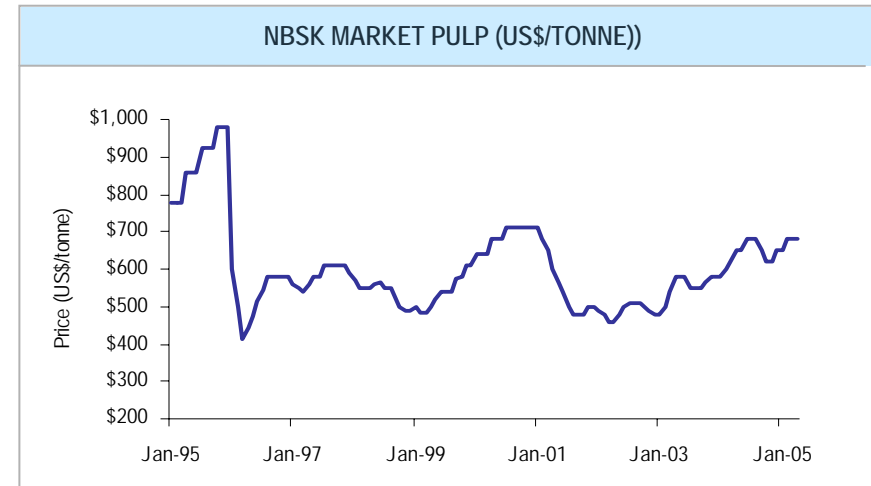
OSB Prices have been Better than Spectacular!

- OSB pricing in C\$ has averaged C\$167/msf more than the 10-year average over the past 23 months!
- OSB producers have also benefited from the absence of countervailing and AD duties...
- This has led to spectacular margins resulting in the complete restructuring of several company's balance sheets
- Despite this very positive situation, OSB producers could face strong headwinds if significant new capacity and increasing costs coincide with slowing housing demand



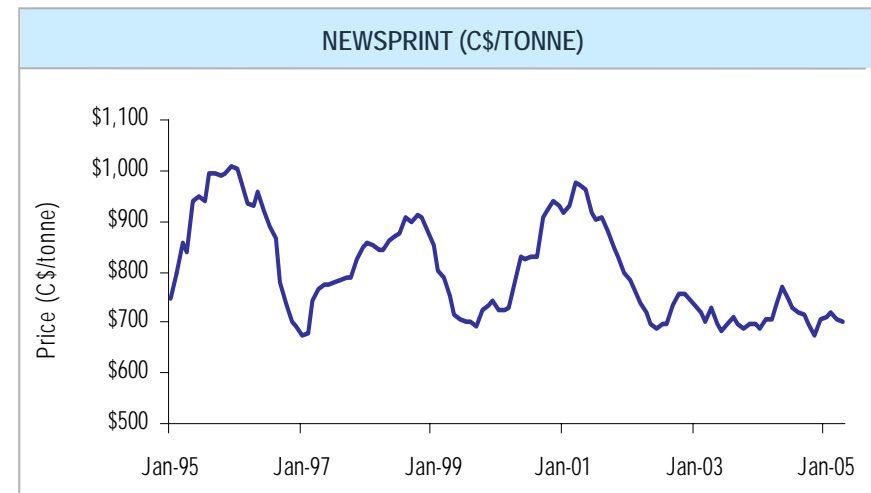
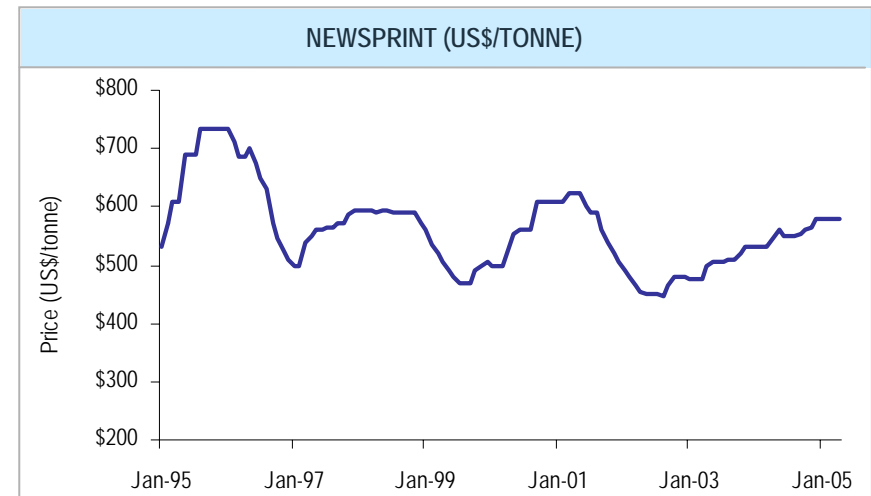
The Story for Market Pulp Producers hasn't Been as Pretty...

- Market pulp prices have averaged C\$68 per tonne less than the 10-year average over the past four years...
- In general, operating rates have been above the 10-year average
- B.C. producers benefit from very low chip costs (currently approximately C\$75 BDU less than eastern Canadian market price)
- With the exception of those lumber producers with high leverage to pulp (CFP and WFT), most market pulp producers face significant financial challenges
- Canadian pulp mills are increasingly uncompetitive as replacement capacity is located in lower cost structured jurisdictions while benefiting from much greater scale



Newsprint has been a Particularly Difficult Commodity

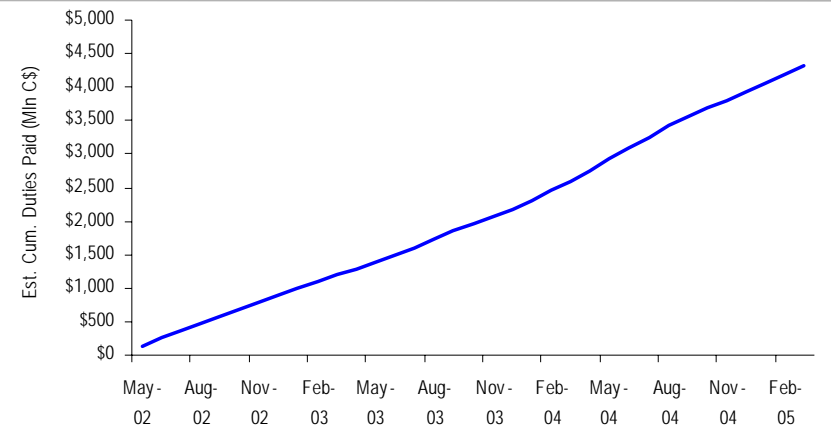
- Newsprint is in secular decline with consumption down almost 20% from the 1999 high
- The increase in the Can\$/US\$ has more than offset the two+ year increase in North American newsprint pricing
- Producers of newsprint and groundwood specialties can expect to face continuous challenges with a run-for-cash, cost-minimization strategy expected to prevail



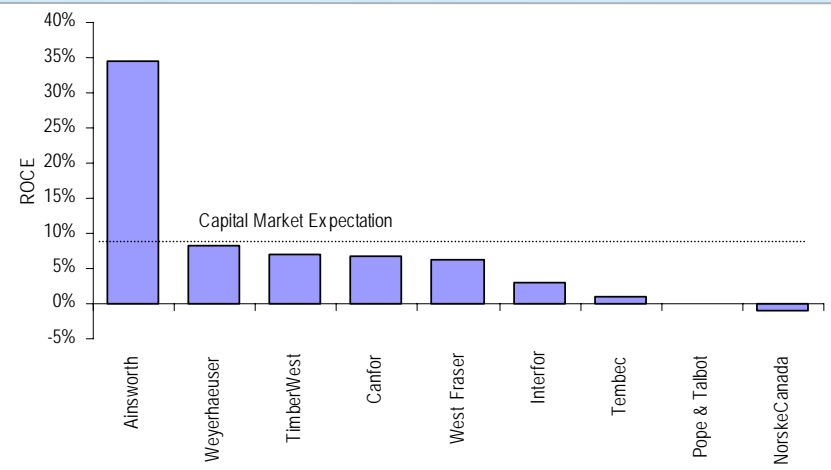
So... How Have We Done?

- Summing it all up...
 - Despite the fact that CVD & AD duties have had a severe impact on earnings, earnings have been good (for wood products producers)
 - Balance Sheets are in mixed condition
 - Wood products prices have been well above trend in C\$
- B.C. Interior producers should be celebrating!
- However...
 - The ROCE employed for the BC forest industry having a \pm \$12 billion total capitalization (excluding Weyerhaeuser and including Tembec) on a capital-weighted basis was only 6.8% in 2004 (blame it on the pulp and paper sector!)
 - Capital market expectation for Canadian P&FP sector is \pm 11%... This suggests approximately \$500 mln in lost capital opportunity in the BC forest industry in 2004!
- Obviously still lots of Room for Improvement!

COUNTERVAILING AND ANTI-DUMPING DUTIES HAVE TAKEN THEIR TOLL

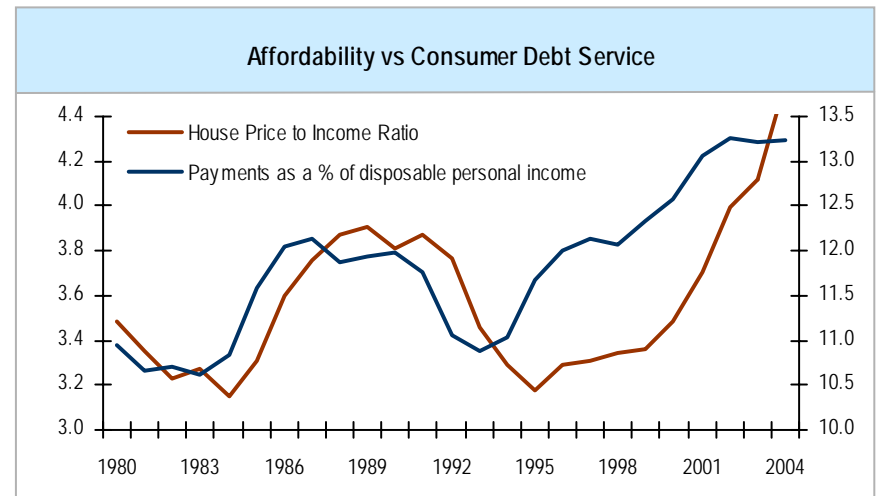
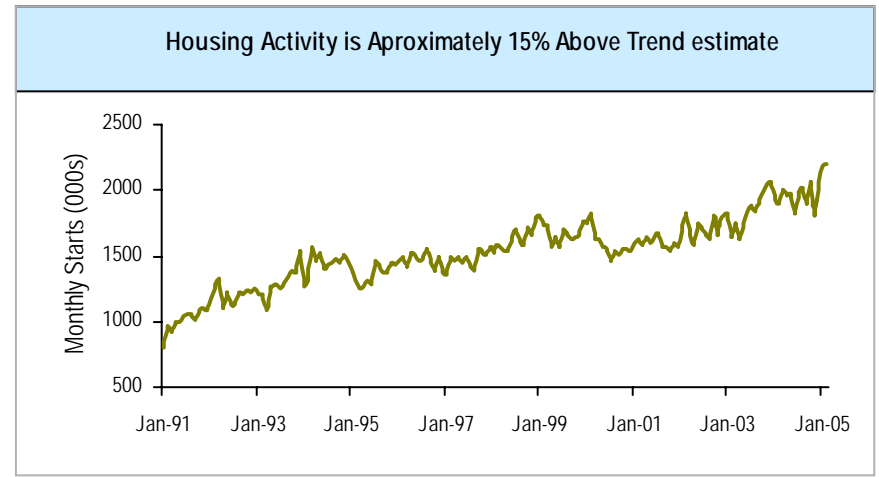


3-YEAR RETURN ON CAPITAL EMPLOYED



What About the Future..?

- Wood Products Demand... No where to go but down!
- Housing starts will slow:
 - Rates are increasing
 - Affordability is a record lows
 - Ownership is at record highs, and
- Consider:
 - In 2004, 23% of all homes purchased in the US were "second homes" for investment purposes
 - Another 13% of all home purchases were "second home" vacation properties
 - Second homes purchased for investment were up 14.4% last year and vacation home purchases surged 19.8% year over year
 - Most individuals now believe real estate is a good investment - public money always chases the inflating asset, until it stops inflating, of course!
 - US House prices were up 11% in 2004
- Slowing market will lead to surplus supply – pricing will move to marginal supplier's cost.
 - Devastating to eastern lumber producers
 - Damaging to BC lumber producers



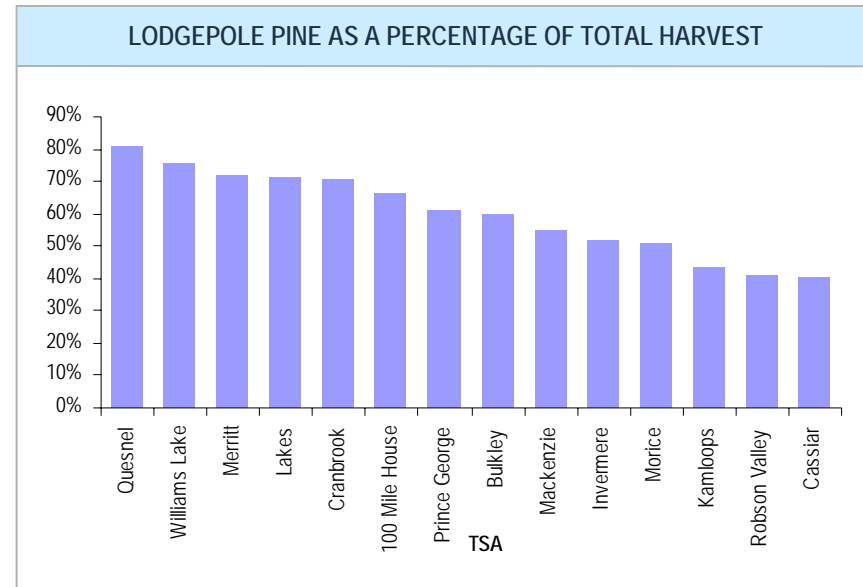
Planning for the Future – Mountain Pine Beetle

- Current analysis suggests 60 to 80% of the mature Pine in the Interior of British Columbia will be dead within the next 3 to 5 years
- The present AAC for the area is 49.2 million m³ with more upward revisions possible in the future.
- Assuming 70% of mature Pine is killed suggests the AAC in the affected area will be reduced to 26.7 million m³ 10 to 15 years from now.
- Based on current estimated log consumption in the area, this reduced cut will mean:
 - Closure of up to 25 sawmills equivalent to approximately 3.5 BBF of annual lumber production
 - 1.8 million ODT's of by-product chips (enough to supply three 1,000 tonne/day Pulp Mills).



Planning for the Future – Mountain Pine Beetle

- Lodgepole Pine accounts for approximately 45% of the Interior harvest
- Impact will be greatest in the Highway 97 / Highway 16 corridor
- Little or no opportunity to mitigate impacts expected to last over 40 years
- Time for rational strategies



	Pre-Beetle / Fire AAC	Current AAC	Pine % of THLB	Post Beetle AAC	Estimated Log Consumption	(Shortfall) / Surplus
Kamloops / Okanagan	8,234,970	10,104,970	36%	6,172,200	8,688,400	(2,516,200)
Hwy 97 / Hwy 16 Corridor	21,563,417	33,193,117	38%	15,873,700	27,651,900	(11,778,200)
Headwaters / Columbia / Kootenay	5,796,247	5,866,247	28%	4,651,800	6,613,200	(1,961,400)

Mountain Pine Beetle - What is a Company to Do?

- The Forest industry does not have mobile assets
- Producers in affected regions have only two obvious options:
 - Run for cash, amortize soon-to-be redundant mills, reduce enterprise value by paying down debt and paying out dividends (may reflect a belief that company can be a successful survivor)
 - Take profits and reinvest outside of affected region
- If Option 1 is the choice there is little strategic imperative – stay the course and focus on the business
- Strategy for Option 2 requires taking every action to reduce cost of capital while building the expertise to explore business opportunities in new jurisdictions...
 - Successful strategies outside of B.C. and Alberta have remained new territory for most firms
- Preparing for the EXTREME community level social implications of the pine beetle infestation will be just as important as a company's investment and operating strategies



Synopsis...

Things are OK Now...

- Coastal industry has huge challenges but is rapidly moving into a 2nd growth world with improved ownership and improving opportunities for reform
- Interior industry could have a decent 5 - 8 years ahead owing to high volumes and low stumpage associated with beetle wood
- Pulp and paper look like no fun...
- Regulatory toolbox and general business environment have improved markedly over past four years

Major Challenges for the Future Include:

- Market Access
- Increasing challenges accessing capital
- Long-term fibre supply in Interior
- Prices for residuals are expected to continue to decline as pulp and paper industries' ability to pay deteriorates
- First Nations uncertainties
- Community impacts of harvest reductions in the Interior

No Time to Coast!!!



Get Used to Running Flat Out While Looking Over Your Shoulder!!!